

2987

No. 15339

United States
Court of Appeals
for the Ninth Circuit

AMERICAN TRUST COMPANY, a Corporation,
Appellant,

vs.

JAMES G. SMYTH, Collector of Internal Revenue
and UNITED STATES OF AMERICA,
Appellees.

Transcript of Record

Appeal from the United States District Court for the
Northern District of California,
Southern Division.

FILED

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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in italic; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in italic the two words between which the omission seems to occur.]

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In the United States District Court for the Northern District of California, Southern Division

No. 33,507

AMERICAN TRUST COMPANY, a Corporation,
as Trustee,

Plaintiff,

vs.

JAMES G. SMYTH, Collector of Internal Revenue,
and the UNITED STATES OF AMERICA,

Defendants.

COMPLAINT

Plaintiff American Trust Company, a corporation, for its complaint alleges:

First Claim for Relief Against the Defendant
James G. Smyth, Formerly Collector of Internal Revenue.

1. This action is brought to recover Federal income taxes erroneously and illegally collected by the defendant James G. Smyth from the plaintiff. The action arises under Sections 22 (b) (7), 322, 3771 and 3772 of the Internal Revenue Code, and this Court has jurisdiction of this action by virtue of 28 United States Code, Sections 1331 and 1340.

2. The plaintiff, American Trust Company, now is and at all times herein mentioned has been a corporation organized under the laws of California, with its principal place of business located in San

Francisco, California. As such it is and has been authorized to act as trustee of express trusts, and since February 28, 1938, it has been trustee of a certain testamentary trust created by Harry L. Tevis, who died on July 19, 1931.

3. Defendant James G. Smyth was at all times since May 14, 1945, and until September 27, 1951, the Collector of Internal Revenue for the First District of California. On September 27, 1951, said defendant retired from office as Collector of Internal Revenue and is not now in such office, but is still alive and resides within the territorial jurisdiction of this Court.

4. During the year 1946 the plaintiff as trustee of the Tevis trust sold certain shares of the corporate stock of Kern County Land Co., a corporation, and certain other securities which comprised part of the corpus of such trust, and on such sales realized capital gains or profits in the aggregate sum of \$1,141,915.72. Under the provisions of California law these gains and profits were not distributable to the life beneficiaries of the trust, but the entire proceeds of the sales were required to be and were retained by the trustee as part of the corpus of the trust.

5. On or about March 14, 1947, plaintiff as trustee of the said trust duly filed a Federal Fiduciary Income Tax Return for the calendar year 1946 with the Collector of Internal Revenue for the First District of California, in which were reported the

transactions described in paragraph 4 above. Thereafter and on the dates and in the amounts hereinafter set forth, defendant James G. Smyth, as Collector of Internal Revenue, collected from the plaintiff, and the plaintiff, acting as the trustee of the aforesaid trust, overpaid to the defendant as Collector of Internal Revenue, in respect of income taxes reported on said Return, \$570,957.86 in quarterly installments as follows:

March 14, 1947	\$142,739.48
June 9, 1947	142,739.46
September 8, 1947	142,739.46
December 11, 1947	142,739.46

6. Thereafter, on or about November 28, 1949, the plaintiff as trustee of the aforesaid trust duly filed a claim for refund with the Commissioner of Internal Revenue, contending that such amounts aggregating \$570,957.86 were erroneously and illegally collected by the defendant James G. Smyth as Collector of Internal Revenue. The said claim for refund set forth the same grounds for refund as are set forth in the complaint herein.

7. On or about April 25, 1952, the Commissioner of Internal Revenue mailed to plaintiff by registered mail a notice of the disallowance in full of plaintiff's claim for refund. No part of said \$570,957.86 with interest thereon as provided by law has ever been refunded to plaintiff.

8. On July 19, 1931, Harry L. Tevis, late of the County of Santa Clara, State of California, died

testate. Pursuant to proceedings duly had and taken in the Superior Court of the State of California in and for the County of Santa Clara, on August 19, 1931, the Superior Court duly made and rendered its order, admitting the will of the decedent, Harry L. Tevis, to probate, and on July 26, 1935, duly made and rendered a final decree of distribution ordering the distribution by the executors to the trustees of the several trusts created under the will of Harry L. Tevis, and such a distribution to such trustees was duly made.

9. Harry L. Tevis died unmarried and without children. Under his will, Harry L. Tevis bequeathed certain specific legacies in cash to named individuals, created four trusts in equal amount for each of the four sons of his brother, William S. Tevis, and a trust in equal amount for one Edwin Lee Dunlap. By paragraph Seventh of his will all the rest and residue of any and all property owned by decedent at his death was bequeathed as follows:

(a) One-half to the decedent's niece, Florence Fermor-Hesketh;

(b) all of the remaining one-half not disposed of as set forth in subparagraph (c) below in trust for the children of Florence Fermor-Hesketh born before decedent's death, with remainders over, the terms of said trust being set forth in paragraph 11 of this complaint;

(c) out of the one-half not disposed of to Florence Fermor-Hesketh, a named sum in trust for the

decedent's brother, William S. Tevis, with remainders over to decedent's four nephews, the sons of his brother William.

10. In his will, Harry L. Tevis named one Fred T. Elsey as trustee of each of the trusts set up under the will and named the plaintiff as successor trustee. Said Fred T. Elsey duly qualified and served as trustee until February 28, 1938, when such trustee ceased to act as trustee. In pursuance of proceedings duly had and taken in said Superior Court for the County of Santa Clara, such Court issued an order duly made and rendered, confirming the appointment of the plaintiff as successor trustee of the trusts set up under paragraph Seventh, subdivision (b), of the said will of Harry L. Tevis, and since then plaintiff has been the duly qualified and acting trustee of such trust, and has held and possessed the corporate shares and securities constituting the corpus of such trust, including the shares and securities sold within the year 1946 as set forth in paragraph 4 above.

11. The said final decree of distribution made and rendered by the said Superior Court on July 26, 1935, incorporated the said will of Harry L. Tevis and distributed a portion of the property of said decedent in accordance with subparagraph (b) of paragraph Seventh of said will. Said subparagraph (b) of paragraph Seventh read and reads as follows:

“(b) All that part of the remaining one-half thereof which is not disposed of by the provisions

of subdivision (c) of this paragraph (Seventh) I give, devise and bequeath to Fred T. Elsey, as Trustee, upon the uses and trusts, and for the purposes and with the powers hereinafter specified, namely:

“To receive the rents, issues and profits and income of the trust estate, and to pay the net rents, issues, profits and income therefrom in equal shares to the children of my niece Florence Fermor-Hesketh born before my death, or to the survivor or survivors of them, during their lives, respectively.

“If any of the said children of my said niece, Florence Fermor-Hesketh, shall have predeceased me, leaving issue living at my death, my said trustee shall forthwith transfer, pay over and deliver to the said issue of each of said children who predeceases me (and there is hereby given, devised and bequeathed to the issue living at my death of each of said children of my said niece who shall predecease me) one of as many portions of the said corpus of the trust aforesaid as shall be ascertained by adding together the number of the children of my said niece living at my death and the number of her children who predecease me leaving issue living at my death.

“If after my death any of the said children of my niece born before my death shall die leaving issue, then there shall be transferred, paid over and delivered to such issue (and in that event there is hereby given, devised and bequeathed to such issue)

one of as many parts of the aforesaid trust fund as shall be ascertained by adding together the number of the children of my said niece living at my death and the number of her children who predecease me leaving issue living at my death.

“If upon the death of the last of the children of my said niece born before my death and after the issue of each of them who left issue either living at my death, or born thereafter, shall have received the portion of the trust fund which it is hereinabove provided shall be delivered to them, there shall be any overplus in the hands of such trustee, said overplus shall be then transferred, paid over and delivered (and, in that event, there is hereby given, devised and bequeathed) to the then living issue of the said children of my said niece in equal shares per capita and not per stirpes.”

12. By paragraph Tenth of the will of Harry L. Tevis it was provided that:

“The word ‘children’ wherever used in this will means and includes only the first generation of direct lineal descendants. The word ‘issue’ wherever used in this will means and includes direct lineal descendants of all generations.”

13. Florence Fermor-Hesketh, the decedent's niece, has had five children, all of whom were born prior to the decedent's death, namely, Thomas S. Fermor-Hesketh, born October 7, 1910; Louise Fermor-Hesketh Stockdale, born December 15, 1911; Flora Fermor-Hesketh Lawson, born February 23,

1913; Frederick Fermor-Hesketh, born April 8, 1916; and John Breckenridge Fermor-Hesketh, born March 7, 1917. Thomas S. Fermor-Hesketh died on June 21, 1937, without issue. The decedent's niece, Florence Fermor-Hesketh, had no child or children who predeceased the decedent, and at the time of the decedent's death no child of Florence Fermor-Hesketh had predeceased the decedent leaving issue living at the decedent's death.

14. During the calendar year 1946 the living direct lineal descendants of the children of Florence Fermor-Hesketh were: the two children of Louise Fermor-Hesketh Stockdale, namely: Ann Louise Stockdale, born May 30, 1938, and Thomas Stockdale, born January 7, 1940; and the three children of Florence Fermor-Hesketh Lawson, namely: John Baring, born August 16, 1934; James Baring, born August 16, 1938 (sons by a former marriage), and Arabella Ann Lawson, born August 14, 1946. All of these direct lineal descendants were and are unmarried.

15. Thomas S. Fermor-Hesketh until his death and each of the four living children of Florence Fermor-Hesketh born prior to the decedent's death named in paragraph 13 above and each of the children of such children named in paragraph 14 above were at the date of the decedent's death and continuously have been since such death residents of the United Kingdom of Great Britain and Ireland not engaged in trade or business in the United States, within the meaning of a certain treaty or

Tax Convention between the Government of the United States and the Government of the United Kingdom proclaimed by the President of the United States on July 30, 1946, and effective January 1, 1945 (60 Stats. 1377).

16. The four living children of Florence Fermor-Hesketh and the grandchildren of Florence Fermor-Hesketh named in paragraphs 13 and 14 above were all born domiciled in and subjects and residents of the United Kingdom; since the dates of their respective births they have continued to be domiciled in and subjects and residents of the United Kingdom; they have lived continuously in the United Kingdom; their interests and affairs have all centered in the United Kingdom; their present intention is to remain domiciled in and subjects and residents of the United Kingdom indefinitely, and there is no likelihood that prior to the respective deaths of the four children of Florence Fermor-Hesketh such children and the five grandchildren of Florence Fermor-Hesketh will not remain domiciled in and subjects and residents of the United Kingdom.

17. The United States income taxes amounting to \$570,957.86 collected from the plaintiff as trustee under the aforesaid trust by the defendant James G. Smyth as Collector of Internal Revenue were erroneously and illegally collected and are refundable to the plaintiff. The gain or profit on the sale of the trust securities made by the plaintiff as

trustee in 1946 amounting to \$1,141,915.72 was not subject to United States income taxes, but, on the contrary, such gain was expressly freed from the burden of and made exempt from any and all United States taxes under the provisions of Section 22 (b) (7) of the Internal Revenue Code which exempts income of any kind to the extent required by any treaty of the United States, including the aforesaid Treaty between the Government of the United States and the Government of the United Kingdom, proclaimed by the President of the United States on July 30, 1946. Article XIV of the aforesaid Treaty provides:

“A resident of the United Kingdom not engaged in trade or business in the United States shall be exempt from United States taxes on gains from the sale or exchange of capital assets.”

18. In making the sales resulting in such aforesaid capital gains the plaintiff as trustee was acting in a fiduciary capacity. Under the terms of the trust and the law of California, the proceeds from the sales were required to be and were retained as part of the corpus of the trust, and income taxes, if any, arising from such sales were chargeable against the corpus of the trust. The income taxes collected by the said Collector of Internal Revenue on the aforesaid sales constituted an illegal and unwarrantable burden on residents of the United Kingdom not engaged in trade or business in the United States, in direct violation of Section 22 (b)

(7) of the Internal Revenue Code, as particularized by Article XIV of the aforesaid treaty, which relieves such residents from United States taxes on gains from the sale of capital assets whether such assets are directly owned or are held beneficially for such residents under an express trust, and also in violation of the requirements of the aforesaid treaty guaranteeing reciprocity of treatment in respect of capital gains by the subjects and citizens of the two contracting parties, whether the property giving rise to such capital gains is directly owned or is held beneficially for such residents under an express trust.

19. At all times material to this action, under the laws of the United Kingdom gains on the sale of capital assets, including gains on the sale by a trustee of an express trust of securities constituting the corpus of such trust, were and are exempt from any income taxes imposed by the United Kingdom, except in the narrow case where the seller is a "trader" in securities not here applicable. The generally accepted meaning of the word "exempt" in the United States and in the United Kingdom, as defined in American and British standard dictionaries of the English language, is to free from, as from some liability or burden, or not made subject to a charge, payment or tax.

20. The defendant James G. Smyth is indebted to plaintiff, as trustee for the beneficiaries of said trust, in the sum of \$570,957.86, with interest

thereon as provided by law, no part of which has been paid.

Second and Alternative Claim for Relief Against the Defendant, the United States of America.

1. This action is brought to recover federal income taxes erroneously and illegally collected by the defendant James G. Smyth from plaintiff and by him paid to the defendant United States of America. This action arises under Sections 22 (b) (7), 322, 3771 and 3772 of the Internal Revenue Code, and this Court has jurisdiction of this action by virtue of 28 United States Code, Sections 1331, 1340 and 1346. The claim is in substitution for the claim against the defendant James G. Smyth as Collector of Internal Revenue and is authorized under 28 United States Code, Section 1346, since such Collector has retired and is not now in office at the institution of the suit.

2. Plaintiff herein incorporates by reference all the allegations of paragraphs 2, 3, 4, 5, 6, 7, 8, 9, 10, 11, 12, 13, 14, 15, 16, 17, 18 and 19 of the First Claim for Relief.

3. The defendant United States of America is indebted to plaintiff, as trustee for the beneficiaries of said trust, in the sum of \$570,957.86, with interest thereon as provided by law, no part of which has been paid.

Third and Alternative Claim for Relief Against the Defendant, the United States of America.

1. This action is brought to recover federal income taxes erroneously and illegally collected by the defendant James G. Smyth from plaintiff and by him paid to the defendant United States of America. This action arises under Sections 22 (b) (7), 322, 3771 and 3772 of the Internal Revenue Code, and this Court has jurisdiction of this action by virtue of 28 United States Code, Section 1346.

2. Plaintiff incorporates herein by reference all of the allegations of paragraphs 2, 3, 4, 5, 6, 7, 8, 9, 10, 11, 12, 13, 14, 15, 16, 17, 18 and 19 of the First Claim for Relief.

3. The defendant United States of America is indebted to the plaintiff as trustee for the beneficiaries of said trust in the sum of \$570,957.86, with interest thereon as provided by law, no part of which has been paid.

Wherefore, the plaintiff demands judgment:

(1) On the first claim for relief against the defendant James G. Smyth, former Collector of Internal Revenue, for \$570,957.86, interest, costs and general relief;

(2) In the alternative, on the second claim for relief against the defendant, the United States of America, for \$570,957.86, interest, costs and general relief;

(3) In the alternative, on the third claim for relief against the defendant, the United States of America, for \$570,957.86, interest, costs and general relief.

/s/ HOWARD J. FINN,

/s/ THEODORE R. MEYER,

BROBECK, PHLEGER &
HARRISON,

Attorneys for Plaintiff.

/s/ MONTGOMERY B. ANGELL,

DAVIS, POLK, WARDELL,
SUNDERLAND & KIENDL,

Of Counsel.

[Endorsed]: Filed April 21, 1954.

[Title of District Court and Cause.]

DEFENDANTS' ANSWER TO PLAINTIFF'S
COMPLAINT

The defendant, James G. Smyth, Collector of Internal Revenue, and the defendant, the United States of America, by their attorney, Lloyd H. Burke, United States Attorney, in and for the Northern District of California, Southern Division, for their answer to plaintiff's complaint herein, admit, deny and allege as follows:

First Claim Against the Defendant James G. Smyth

1. The allegations in Paragraph 1 are admitted except that it is denied that the income taxes involved were erroneously or illegally collected.

2. The allegations in Paragraph 2 are admitted.

3. The allegations in Paragraph 3 are admitted.

4. The allegations in Paragraph 4 are admitted.

5. The allegations in paragraph 5 are admitted except that it is denied that the plaintiff acting as trustee of the aforesaid trust overpaid said taxes, but defendants allege that on the contrary said taxes were properly and legally paid and collected and were due and owing at the time of the payment thereof by the plaintiff.

6. The allegations in Paragraph 6 are admitted except that it is denied that the amounts involved or any part thereof were erroneously or illegally collected.

7. The allegations in Paragraph 7 are admitted.

8. The allegations in Paragraph 8 are admitted.

9. The allegations in Paragraph 9 are admitted.

10. The allegations in Paragraph 10 are admitted.

11. The allegations in Paragraph 11 are admitted.

12. The allegations in Paragraph 12 are admitted.

13. The allegations in Paragraph 13 are admitted.

14. The allegations in Paragraph 14 are admitted.

15. The allegations in Paragraph 15 are admitted, except that it is denied that the treaty or tax convention referred to has any application to the parties mentioned and referred to in said paragraph or that said parties fall within any the provisions of the treaty or tax convention under the facts in this case.

16. The allegations in Paragraph 16 are admitted except that the defendants have insufficient knowledge or information upon which to form a belief as to the present intention of said parties to remain domiciled in and subjects and residents of the United Kingdom indefinitely or that there is no likelihood that prior to the respective deaths of the four children and five grandchildren referred to said children and grandchildren will not remain domiciled in and subjects and residents of the United Kingdom.

17. The allegations in Paragraph 17 are denied.

18. The allegations in Paragraph 18 are denied except that it is admitted that plaintiff acted as trustee under the provisions of the will of said Harry L. Tevis, aforesaid, and that under the terms of the trust and the laws of California the proceeds from the sales were required to be and were retained as part of the corpus of the trust and that income taxes arising from such sales were chargeable against the corpus of the trust.

19. Answering Paragraph 19 defendants have insufficient knowledge or information upon which

to form a belief as to the correctness of the allegations set forth therein. Defendants deny that the meaning of the word "exempt" has the meaning attributed thereto by the plaintiff insofar as the interpretation of Article XIV of the treaty between the United States and the United Kingdom is concerned.

20. The allegations in Paragraph 20 are denied.

Second Alternative Claim for Relief Against the
Defendant, the United States of America

1. The allegations in Paragraph 1 are admitted except that it is denied that the income taxes referred to were erroneously or illegally collected by the defendant, James G. Smyth.

2. Defendants incorporate by reference all of the allegations of Paragraphs 2, 3, 4, 5, 6, 7, 8, 9, 10, 11, 12, 13, 14, 15, 16, 17, 18 and 19 of their answer to the corresponding paragraphs of the First Claim for Relief.

3. The allegations in Paragraph 3 are denied.

Third and Alternative Claim for Relief Against the
Defendant, the United States of America

1. The allegations in Paragraph 1 are admitted except that it is denied that the income taxes were erroneously or illegally collected by the defendant, James G. Smyth.

2. Defendants incorporate herein by reference all of their allegations in Paragraphs 2 to 19, in-

clusive, of their answer to corresponding paragraphs of plaintiff's First Claim for Relief.

3. The allegations in Paragraph 3 are denied.

Defendants specifically deny each and every allegation in plaintiff's complaint herein not specifically admitted or qualified herein.

Wherefore, defendants pray that the complaint be dismissed; that defendants have judgment for costs and for all just and proper relief.

/s/ LLOYD H. BURKE,
United States Attorney.

Affidavit of Mail attached.

[Endorsed]: Filed August 17, 1954.

[Title of District Court and Cause.]

STIPULATION No. 2

Subject to the approval of the Court, it is hereby stipulated by the parties, through their respective attorneys, that the complaint herein is hereby amended as follows:

1. Paragraph 4 of the complaint is amended so that it reads:

"4. During the year 1946 the plaintiff as trustee of the Tevis trust sold certain shares of the corporate stock of Kern County Land Co., a corporation, and certain other securities which comprised

part of the corpus of such trust, and on such sales realized gross long term capital gains of \$2,302,733.54 and net long term capital gains taken into account in the aggregate sum of \$1,141,915.72. Under the provisions of California law these gains and profits were not distributable to the life beneficiaries of the trust, but the entire proceeds of the sales were required to be and were retained by the trustee as part of the corpus of the trust.”

As so amended, the defendants and each of them admit the allegations of Paragraph 4.

2. Paragraph 17 of the complaint is amended so that it reads:

“17. The United States income taxes amounting to \$570,957.86 collected from the plaintiff as trustee under the aforesaid trust by the defendant James G. Smyth as Collector of Internal Revenue were erroneously and illegally collected and are refundable to the plaintiff. The net gain or profit taken into account on the sale of the trust securities made by the plaintiff as trustee in 1946 amounting to \$1,141,915.72 was not subject to United States income taxes, but, on the contrary, such gain was expressly freed from the burden of and made exempt from any and all United States taxes under the provisions of Section 22 (b) (7) of the Internal Revenue Code which exempts income of any kind to the extent required by any treaty of the United States, including the aforesaid Treaty between the Government of the United States and the Govern-

ment of the United Kingdom, proclaimed by the President of the United States on July 30, 1946.

Article XIV of the aforesaid Treaty provides:

“ ‘A resident of the United Kingdom not engaged in trade or business in the United States shall be exempt from United States taxes on gains from the sale or exchange of capital assets.’ ”

As so amended, the defendants and each of them deny the allegations of Paragraph 17, except that it is admitted that Article XIV of the aforesaid Treaty contains provisions as alleged in Paragraph 17.

3. Paragraph 19 of the complaint is amended so that it reads:

“19. At at times material to this action, under the laws of the United Kingdom gains on the sale of capital assets, including gains on the sale by a trustee of an express trust of securities constituting the corpus of such trust, were and are exempt from any income taxes imposed by the United Kingdom, except in the narrow case where the seller is a ‘trader’ in securities not here applicable. In each of the several Articles of the Income Tax Convention between the United States and the United Kingdom, full reciprocity in treatment is accorded residents of the United Kingdom realizing income from United States sources and residents of the United States realizing income from United King-

dom sources, notwithstanding the differences in the systems of taxation in the United States and in the United Kingdom. The generally accepted meaning of the word 'exempt' in the United States and in the United Kingdom, as defined in American and British standard dictionaries of the English language, is to free from, as from some liability or burden, or not made subject to a charge, payment or tax."

As so amended, the defendants and each of them deny the allegations of Paragraph 19.

March 22, 1955.

/s/ HOWARD J. FINN,

/s/ THEODORE R. MEYER,

BROBECK, PHLEGER &
HARRISON,

Attorneys for Plaintiff.

/s/ MONTGOMERY B. ANGELL,

DAVIS, POLK, WARDWELL,
SUNDERLAND & KIENDL,
Of Counsel.

/s/ LLOYD H. BURKE,

United States Attorney,
Attorneys for the Defendants.

So Ordered.

/s/ OLIVER J. CARTER,

United States District Judge.

[Endorsed]: Filed March 22, 1955.

[Title of District Court and Cause.]

MEMORANDUM FOR JUDGMENT

Plaintiff, as trustee of a testamentary trust, seeks the refund of capital gains taxes paid under protest. The facts are not in dispute. Jurisdiction is necessarily invoked under 28 U.S.C. Section 1346 (a) (1).

In 1946 plaintiff trustee sold part of the property constituting the corpus of the trust at a profit. Defendant Collector of Internal Revenue collected a capital gains tax based on the gain resulting from that sale of trust property. Throughout 1946 all the life beneficiaries of the trust and all the remaindermen of the trust were residents of the United Kingdom of Great Britain and Northern Ireland; therefore plaintiff claims an exemption from United States capital gains tax, by virtue of Article XIV of the Convention between the United States of America and the United Kingdom of Great Britain and Ireland signed April 16, 1945, effective as of January 1, 1945, relating to income taxes (60 Stat. [part 2] 1377), which provides:

“A resident of the United Kingdom not engaged in trade or business in the United States shall be exempt from United States tax on gains from the sale or exchange of capital assets.”

The defendant does not contend that any of the beneficiaries of the trust are engaged in trade or business in the United States. The defendant does

contend that the capital gain which resulted from the sale of trust property in 1946 was not the income of the beneficiaries and remaindermen of the trust, but was income that was taxable to the trustee; the trustee, a California corporation, is not a resident of the United Kingdom and does not qualify for the exemption of Article XIV of the tax convention. This contention of the defendant is based upon a distinction that has long been made in the scheme of taxation of trusts in the United States; that is, that if trust income is currently distributable to the beneficiaries, it is treated as their income and taxable to them, but if trust income is not currently distributable to the beneficiaries under the trust instrument, it is the trustee's income and is taxable to the trustee. One of the leading cases on this doctrine is *Freuler v. Helvering*, 291 U.S. 35, 41, wherein the Supreme Court said this with regard to the sections of the Internal Revenue Act dealing with the taxation of trusts:

“This [the net income of the trust] the fiduciary may be required to accumulate; or, on the other hand, he may be under a duty currently to distribute it. If the latter, then the scheme of the Act is to treat the amount so distributable, not as the trust's income, but as the beneficiary's.”

The Court held, at page 42:

“The test of taxability to the beneficiary is not receipt of income, but the present right to receive it.”

This rule has been followed in numerous later cases. In *Hubbell v. Helvering*, 8th Cir., 70 F. 2d 668, 669, cert. denied, 283 U.S. 840, the court described the holding of the *Freuler* case in this way:

“That decision determines that the entire net income of the trust estate is taxable; that, in determining such net income, the trustee is authorized to make the appropriate deductions allowed by law to other taxpayers; that so much of such net income as is distributable to the beneficiaries is taxable to them; that whether a part of such income is so distributable depends upon the terms of the instrument creating the trust * * *”

And in *Bryant v. Commissioner*, 4th Cir., 185 F. 2d 517, 519, the court said:

“The test of taxability is not the receipt of income but the right to receive it. *Freuler v. Helvering*, 291 U.S. 35, 54 S.Ct. 308, 78 L.Ed. 634, and the right to receive the income of a trust depends upon the terms of the trust instrument and governing state law.” (Citations omitted.)

See also *Peck v. Commissioner*, 2d Cir., 77 F. 2d 857, 858, cert. denied, 296 U.S. 625; *Saulsbury v. United States*, 5th Cir., 199 F. 2d 578.

Under the trust instrument in the case at bar, capital gains are not currently distributable to the beneficiaries; therefore the defendant argues that capital gains are income to the trustee, and are taxable because the trustee is not entitled to the exemption of the tax convention. The defendant

agrees that if capital gains were currently distributable to the beneficiaries under the terms of this trust, such capital gains would be the income of the beneficiaries, and would be exempt from United States tax under the tax convention because the beneficiaries are residents of the United Kingdom.

Plaintiff attempts to meet this main defense by arguing that the United Kingdom tax convention was intended by the contracting parties to override the provisions of domestic law upon which the defendant relies. These provisions are found in Treasury Department regulations made pursuant to Section 62 of the Internal Revenue Code of 1939 (26 U.S.C., 1952 Ed., Sec. 62). These regulations may be found in T.D. 5569, 1947-2 Cum. Bull. 100, 109, 12 F.R. 1236. Plaintiff makes several points in support of its argument, but none of them are persuasive.

Plaintiff argues that Article XIV of the tax convention should be construed to exempt capital gains resulting from the sale of property "in beneficial ownership." In this connection plaintiff emphasizes that the ordinary income of the trust which is distributable to the beneficiaries is less than it would be if the corpus of the trust were not depleted to the extent of the capital gains tax collected by the defendant. But this is the equivalent of arguing that if any burden of a capital gains tax falls upon a resident of the United Kingdom, the exemption of the tax convention applies. There is no warrant in the convention for such an interpretation.

Plaintiff also seeks comfort in dictionary definitions of the word "exempt" to the effect that the word means "to free from the burden of." Here, again, plaintiff would have this Court construe the exemption of Article XIV to apply to any resident of the United Kingdom on whom falls any of the burden of a United States capital gains tax. There is nothing in the tax convention to justify that construction of the word "exempt," and if that was the intention of the parties to the compact, they could easily have so provided.

Plaintiff also contends that the aim of the parties to the tax convention was equality of treatment in the taxation by each party of the nationals of the other party. From this plaintiff argues that because an American beneficiary of a trust held by a United Kingdom trustee would be wholly free from any burden of United Kingdom capital gains tax, that it must have been intended by the parties to the tax convention that in the reverse but like situation of United Kingdom beneficiaries of a trust with an American trustee, such as in the case at bar, that the beneficiaries should be freed from any burden of the United States capital gains tax. But the reason that an American beneficiary of a trust held by a United Kingdom trustee would be free from any burden of United Kingdom capital gains tax is, that there is no capital gains tax in the United Kingdom. One could just as well argue that a resident of the United Kingdom who held stock in an American corporation should be free

from the burden of United States capital gains taxes on sales of corporate property, because an American stockholder in a United Kingdom corporation would not suffer the burden of a United Kingdom capital gains tax on sales of corporate property. This Court is not convinced that perfect equality of tax treatment was accomplished or intended to be accomplished by the tax convention on which plaintiff relies. Tax conventions are the product of long negotiations between the contracting parties. These negotiations usually consist of a series of tax concessions made by each party to the convention; therefore complete reciprocity is seldom possible.

The provision of the tax convention on which plaintiff must base its whole case, provides in substance that a resident of the United Kingdom shall be exempt from United States capital gains tax. No mention is made of trusts. Plaintiff urges this Court to consider the rule of construction of treaties referred to by the Supreme Court in *Factor v. Laubenheimer*, 290 U.S. 276, 293-294:

“* * * if a treaty fairly admits of two constructions, one restricting the rights which may be claimed under it, and the other enlarging it, the more liberal construction is to be preferred.” (Citations omitted.)

But this Court does not agree that Article XIV fairly admits of the construction that income ordinarily taxable to a trustee is to be taxed to bene-

ficiaries. The basic issue here is, who is the taxpayer? It is perfectly reasonable for the defendant to follow United States law in making that initial determination; there is nothing in the tax convention that would warrant the defendant in looking elsewhere for guidance on that point.

Plaintiff has failed to overcome a basic obstacle to recovery in this suit; namely, plaintiff has failed to show that the capital gain which was taxed here, represented income to the beneficiaries of the trust, who are the only persons who can qualify for an exemption under the convention. Plaintiff has not shown anything in the tax convention that requires this Court to find that the parties to the convention intended to treat the trustee's income as that of the beneficiaries in the case of capital gains.

The case of *Lewenhaupt v. Commissioner*, 20 T.C. 151, affirmed per curiam, 221 F. 2d 229 (Cir. 9), is not controlling here because of difference in the language of the Swedish-American Convention construed in that case, and the language of the United Kingdom - American Convention construed in this case.

It is the conclusion of this Court that the capital gain involved in this case represented income to the trustee, and that the trustee does not qualify for any exemption from taxation on that income.

The defendant has moved to strike stipulation No. 4, and portions of stipulation No. 5, upon the ground that they were irrelevant and immaterial.

Ruling on these motions was reserved. The stipulations are relevant and material to plaintiff's theory of the case, and the motion to strike will, therefore, be denied.

Judgment is awarded to defendant, with his costs of suit incurred herein. Counsel for defendants shall present findings, conclusions and a judgment.

Dated: June 4, 1956.

/s/ OLIVER J. CARTER,

United States District Judge.

[Endorsed]: Filed June 5, 1956.

[Title of District Court and Cause.]

FINDINGS OF FACT AND CONCLUSIONS OF LAW

The above-entitled case was tried by this Court without the intervention of a jury. Plaintiff was **represented** by its counsel, Howard J. Finn; Theodore R. Meyer; Brobeck, Phleger & Harrison, San Francisco, California; Montgomery B. Angell, David A. Lindsay, and Davis, Polk, Wardwell, Sunderland & Kiendl, New York City, and the defendants were represented by their counsel, H. Brian Holland, Assistant Attorney General; Andrew D. Sharpe, Homer R. Miller, Attorneys, Department of Justice, and Lloyd H. Burke, United States Attorney, and Lynn J. Gillard, Assistant United States Attorney.

This Court having heard the evidence and having considered the briefs and arguments of counsel and being duly advised in the premises, makes the following findings of fact and conclusions of law, pursuant to Rule 52, Federal Rules of Civil Procedure for District Courts of the United States.

Findings of Fact

1. Plaintiff instituted this action against the defendants to recover \$570,957.86, plus interest, income taxes for the year 1946. The defendants filed an answer denying liability.

2. The sole issue in the case was whether or not the plaintiff was exempt from income taxes on long-term capital gains on the sale of securities, the proceeds of which sale were not distributed as income to the beneficiaries of the trust under which plaintiff was trustee pursuant to California law, but became part of the principal of the trust, where all of the beneficiaries of the trust were aliens residing in the United Kingdom, exemption being claimed by the plaintiff-trustee in view of the provisions of Article XIV of the Income Tax Convention between the United States and the United Kingdom which provides that residents of the United Kingdom not engaged in trade or business in the United States shall be exempt from United States income taxes on capital gains.

3. The plaintiff, American Trust Company, now is and at all times herein mentioned has been a corporation organized under the laws of California,

with its principal place of business located in San Francisco, California. As such it is and has been authorized to act as trustee of express trusts, and since February 28, 1938, it has been trustee of a certain testamentary trust created by Harry L. Tevis, who died on July 19, 1931.

4. Defendant James G. Smyth was at all times since May 14, 1945, and until September 27, 1951, the Collector of Internal Revenue for the First District of California. On September 27, 1951, said defendant retired from office as Collector of Internal Revenue and is not now in such office, but is still alive and resides within the territorial jurisdiction of this Court.

5. During the year 1946, the plaintiff as trustee of the Tevis trust sold certain shares of the corporate stock of Kern County Land Company, a corporation, and certain other securities which comprised part of the corpus of such trust, and on such sales realized gross long-term capital gains of \$2,302,733.54 and net long-term capital gains taken into account in the aggregate sum of \$1,141,915.72. Under the provisions of California law these gains and profits were not distributable to the life beneficiaries of the trust, but the entire proceeds of the sales were required to be and were retained by the trustee as part of the corpus of the trust.

6. On or about March 14, 1947, plaintiff as trustee of the said trust duly filed a federal fiduciary income tax return for the calendar year 1946

with the Collector of Internal Revenue for the First District of California, in which were reported the transactions described in the foregoing paragraph. Thereafter the defendant James G. Smyth as Collector of Internal Revenue collected from the plaintiff and the plaintiff paid to the said defendant as Collector of Internal Revenue the sum of \$570,957.86 reported in said return and paid in quarterly installments as follows:

March 14, 1947	\$142,739.48
June 9, 1947	142,739.46
September 8	142,739.46
December 11, 1947	142,739.46

7. Thereafter on or about November 28, 1949, the plaintiff as trustee of the aforesaid trust duly filed a claim for refund with the Commissioner of Internal Revenue, contending that the sum of \$570,957.86 referred to in the foregoing paragraph was erroneously and illegally collected by the defendant James G. Smyth as Collector of Internal Revenue. The said claim for refund set forth the same grounds for refund as are alleged in the complaint herein.

8. On or about April 25, 1952, the Commissioner of Internal Revenue mailed to plaintiff by registered mail a notice of the disallowance in full of the plaintiff's claim for refund. No part of said \$570,957.86 or interest thereon has ever been refunded to the plaintiff.

9. On July 19, 1931, Harry L. Tevis, late of the

County of Santa Clara, State of California, died testate. Pursuant to proceedings duly had and taken in the Superior Court of the State of California in and for the County of Santa Clara, on August 19, 1931, the Superior Court duly made and rendered its order, admitting the will of the decedent, Harry L. Tevis, to probate, and on July 26, 1935, duly made and rendered a final decree of distribution ordering the distribution by the executors to the trustees of the several trusts created under the will of Harry L. Tevis, and such a distribution to such trustees was duly made.

10. Harry L. Tevis died unmarried and without children. Under his will, decedent bequeathed certain specific legacies in cash to named individuals, created four trusts in equal amount for each of the four sons of his brother, William S. Tevis, and a trust in equal amount for one Edwin Lee Dunlap. By paragraph Seventh of his will all the rest and residue of any and all property owned by decedent at his death was bequeathed as follows:

(a) One-half to the decedent's niece, Florence Fermor-Hesketh;

(b) All of the remaining one-half not disposed of as set forth in subparagraph (c) below in trust for the children of Florence Fermor-Hesketh born before decedent's death, with remainders over, the terms of said trust being set forth in paragraph 11 of the plaintiff's complaint and admitted in the defendants' answer;

(c) Out of the one-half not disposed of to Florence Fermor-Hesketh, a named sum in trust for the decedent's brother, William S. Tevis, with remainders over to decedent's four nephews, the sons of his brother William.

11. In his will, Harry L. Tevis named one Fred T. Elsey as trustee of each of the trusts set up under the will and named the plaintiff as successor trustee. Said Fred T. Elsey duly qualified and served as trustee until February 28, 1938, when he ceased to act as trustee and pursuant to proceedings duly had taken in the Superior Court for the County of Santa Clara, California, said Court issued an order duly made and rendered, confirming the appointment of the plaintiff as successor trustee of the trusts set up under paragraph Seventh, subdivision (b), of the said will of Harry L. Tevis, and since then plaintiff has been the duly qualified and acting trustee of such trust, and has held and possessed the corporate shares and securities constituting the corpus of such trust, including the shares and securities sold within the year 1946 as set forth in paragraph 5 above.

12. The said final decree of distribution made and rendered by the said Superior Court on July 26, 1935, incorporated the said will of Harry L. Tevis and distributed a portion of the property of said decedent in accordance with subparagraph (b) of paragraph Seventh of said will. Said subparagraph (b) of paragraph Seventh reads as follows:

All that part of the remaining one-half thereof which is not disposed of by the provisions of subdivision (c) of this paragraph (Seventh) I give, devise and bequeath to Fred T. Elsey, as Trustee, upon the uses and trusts, and for the purposes and with the powers hereinafter specified, namely:

To receive the rents, issues and profits and income of the trust estate, and to pay the net rents, issues, profits and income therefrom in equal shares to the children of my niece Florence Fermor-Hesketh born before my death, or to the survivor or survivors of them, during their lives, respectively.

If any of the said children of my said niece, Florence Fermor-Hesketh shall have predeceased me leaving issue living at my death, my said trustee shall forthwith transfer, pay over and deliver to the said issue of each of said children who predeceases me (and there is hereby given, devised and bequeathed to the issue living at my death of each of said children of my said niece who shall predecease me) one of as many portions of the said corpus of the trust aforesaid as shall be ascertained by adding together the number of the children of my said niece living at my death and the number of her children who predecease me leaving issue living at my death.

If after my death any of the said children of my niece born before my death shall die leaving issue, then there shall be transferred, paid over and delivered to such issue (and in that event there is

hereby given, devised and bequeathed to such issue) one of as many parts of the aforesaid trust fund as shall be ascertained by adding together the number of the children of my niece living at my death and the number of her children who predecease me leaving issue living at my death.

If upon the death of the last of the children of my said niece born before my death and after the issue of each of them who left issue either living at my death, or born thereafter, shall have received the portion of the trust fund which it is hereinabove provided shall be delivered to them, there shall be any overplus in the hands of such trustee, said overplus shall be then transferred, paid over and delivered (and, in that event, there is hereby given, devised and bequeathed) to the then living issue of the said children of my said niece in equal shares per capita and not per stirpes.

13. By paragraph Tenth of the will of Harry L. Tevis it was provided that:

The word "children" wherever used in this will means and includes only the first generation of direct lineal descendants. The word "issue" wherever used in this will means and includes direct lineal descendants of all generations.

14. Florence Fermor-Hesketh, the decedent's niece, has had five children, all of whom were born prior to the decedent's death, namely Thomas S. Fermor-Hesketh, born October 7, 1910; Louise Fermor-Hesketh Stockdale, born December 15,

1911; Flora Fermor-Hesketh Lawson, born February 23, 1913; Frederick Fermor-Hesketh, born April 18, 1916; and John Brekenridge Fermor-Hesketh, born March 7, 1917. Thomas S. Fermor-Hesketh died on June 21, 1937, without issue. The decedent's niece, Florence Fermor-Hesketh, had no child or children who predeceased the decedent, and at the time of the decedent's death no child of Florence Fermor-Hesketh had predeceased the decedent leaving issue living at the decedent's death.

15. During the calendar year 1946 the living direct lineal descendants of the children of Florence Fermor-Hesketh were: the two children of Louise Fermor-Hesketh Stockdale, namely: Ann Louise Stockdale, born May 30, 1938, and Thomas Stockdale, born January 7, 1940; and the three children of Florence Fermor-Hesketh Lawson, namely: John Baring, born August 16, 1934, James Baring, born August 16, 1938 (sons by a former marriage), and Arabella Ann Lawson, born August 14, 1946. All of these direct lineal descendants were and are unmarried.

16. Thomas S. Fermor-Hesketh until his death and each of the four living children of Florence Fermor-Hesketh born prior to the decedent's death named in paragraph 14 above and each of the children of such children named in paragraph 15 above were at the date of the decedent's death and have continuously have been since such death residents of the United Kingdom of Great Britain and

Ireland, and were not engaged in trade or business in the United States.

17. The four living children of Florence Fermor-Hesketh and the grandchildren of Florence Fermor-Hesketh named in paragraphs 14 and 15 above were all born, domiciled in and subjects and residents of the United Kingdom, and since the dates of their respective births they have continued to be domiciled in and are subjects and residents of the United Kingdom, and they have lived continuously in said United Kingdom.

18. Article XIV of the Income Tax Convention between the United States of America and the United Kingdom, proclaimed by the President of the United States on July 30, 1946, and effective January 1, 1945 (60 Stats. 1377), provides as follows:

“A resident of the United Kingdom not engaged in trade or business in the United States shall be exempt from United States taxes on gains from the sale or exchange of capital assets.”

19. Under the terms of the Harry L. Tevis trust under which plaintiff was acting as trustee and under the laws of the State of California, the proceeds from the sales of the securities involved herein were required to be and were retained as part of the corpus of the trust, and income taxes, if any, arising from such sales were chargeable against the corpus of the trust.

20. The securities comprising part of the corpus of the Tevis trust which were sold in 1946 by the plaintiff as trustee of such trust, constituted capital assets. The capital gains realized on the sale of such securities held for more than six months amounted to \$2,302,733.54, and, after adjustments on account of certain long and short term capital losses in respect to other securities sold and the application of the capital loss carried over from 1945, the net capital gain taken into account on account of such sales amounted to \$1,141,915.72.

21. The sales made by the plaintiff as trustee in 1946 consisted mainly of 57,200 shares of Kern County Land Company stock which sales the trustee realized \$2,574,000 in cash.

22. The corpus of the trust created under paragraph Seventh of the will of Harry L. Tevis constituted the portion of the property of the decedent distributed to the trustee of such trust under the final decree of the Superior Court of Santa Clara County dated July 26, 1935.

23. The children of Florence Fermor-Hesketh set forth in paragraph 14 herein and the grandchildren of Florence Fermor-Hesketh set forth in paragraph 15 herein were in 1946 and always have been citizens of the United Kingdom of Great Britain and Northern Ireland, and were not in 1946 and never have been citizens of the United States; such children and grandchildren were in 1946 and always have been resident in the United Kingdom

for the purposes of the United Kingdom income tax, and were not in 1946 and never have been resident in the United States for the purposes of the United States income tax; such children and grandchildren were not and never have been engaged in trade or business in the United States; and such children and grandchildren did not have in 1946 and never have had a permanent establishment situated within the United States.

24. The present Fermor-Hesketh family grew out of the union in 1846 of two old English families, namely, the Hesketh family and the Fermor family. In 1946 Lady Anna Maria Arabella Fermor married Sir Thomas George Hesketh, and by Royal License dated November 8, 1867, Sir Thomas Hesketh and his son, Thomas George, were authorized to take the surname of Fermor, and from such date their descendants have borne the name of Fermor - Hesketh. Florence Former - Hesketh was born in California on December 31, 1881, the daughter of the late John Witherspoon Breckenridge of California. In 1909 she was married to Sir Thomas Fermor-Hesketh, Baronet, an English citizen and resident in England and since her marriage she has been a citizen of the United Kingdom and resides in Northhamptonshire, United Kingdom. Her husband died on July 20, 1944.

Louise Fermor-Hesketh Stockdale her daughter was born in England on December 15, 1911, was educated in England and has lived all of her life in England. On July 24, 1937, she married Edmund

Villiers Minshull Stockdale, a citizen of the United Kingdom whose family has always resided in Northamptonshire, and who is a banker and stockbroker, a Justice of the Peace and a Sheriff in the City of London. All of his relatives are resident in England and his close friends and the friends of his wife are all English people. The two now occupy an estate in Hampshire comprising substantial land holdings and their three children are now being educated in English schools.

Flora Fermor-Hesketh Lawson was born in England on February 23, 1913. She was educated in England and has lived all of her life in England. In 1934 she married Rupert Baring, Baron Revelstoke, a citizen of the United Kingdom and the two sons of this marriage are now being educated at Eton College. The Revelstokes lived in London until Flora Fermor-Hesketh Lawson divorced her husband in 1944. Baron Revelstoke has never remarried. The two sons are the sole heirs of their father. Following the divorce, Flora Fermor-Hesketh Lawson married Commander Arnold Derek Arthur Lawson, a citizen of the United Kingdom who has always resided in England, and she has had two daughters by this marriage both born in London and who have always lived in England. Since their marriage, the Lawsons have acquired substantial properties and a residence in Buckinghamshire, England. Mr. Lawson was a former solicitor in London, but has now retired. The close friends and relatives of Baron Revelstoke and of the Lawsons all reside in England.

Frederick Fermor-Hesketh was born in England in 1916, has always resided in England and was educated at schools and colleges in England. In 1949 he married Christian Mary McEwen, a citizen of the United Kingdom and a resident of England. The three children by this marriage have always lived in England.

John Breckenridge Fermor-Hesketh was born in England in 1917 and since his birth has been a citizen of the United Kingdom and a resident of England. He was educated in schools and colleges in England, and in 1946 he married Patricia Macaskie Cole, an English citizen and a resident of England. They have no children. Most of the friends of Mr. and Mrs. John Breckenridge Fermor-Hesketh reside in England. Since 1946 Mr. Fermor-Hesketh, sometimes accompanied by his wife, has spent two or three months each year in California looking after certain of his mother's affairs.

With the exception of John Breckenridge Fermor-Hesketh, the business connections of the members of the Fermor-Hesketh family noted above are almost wholly limited to the United Kingdom and the close friends and members of the Fermor-Hesketh family reside in and are citizens of the United Kingdom. John Breckenridge Fermor-Hesketh has some business interests and friends in California. The bulk of his business connections are in England, and his close friends reside in and are citizens of the United Kingdom.

25. Following the sales of the securities constituting part of the Tevis trust as made by the plaintiff in 1946 as trustee of such trust, the plaintiff as trustee reinvested the cash proceeds (after setting aside an amount sufficient to pay the expenses of and the taxes on such sales) in securities which were held as part of the corpus of the trust fund. The average rate of return on the securities purchased out of such proceeds of sale for the succeeding seven year period 1947-1953, inclusive, was approximately 3.84%.

26. During 1944 and 1945 and at all times thereafter, the United Kingdom income tax and the United Kingdom surtax were charged upon annual income derived by any person residing in the United Kingdom from any source whatever, and upon annual income derived by any person from sources within the United Kingdom whether or not the resident was a British subject or a resident of the United Kingdom.

27. During 1944 and 1945 and at all times thereafter, under the system of income taxation in the United Kingdom of Great Britain and Northern Ireland a charge or tax is imposed upon income but not upon realized accretions of capital; a resident or non-resident individual, a corporation or a trustee of an express trust who realizes gains or profits on the sale of securities or real and other property in the United Kingdom is not chargeable with income tax (including surtax), the excess profits tax or the national defense contribution (in 1946 re-

named the profits tax) unless what is done is not merely a realization or change in investment but an act done in what is truly the carrying on or carrying out of a business; subject to the foregoing, an accretion of capital is not taxable merely because the original capital was invested in the hope and expectation that it would rise in value, and if it does rise in value the realization on a sale does not result in taxable income.

28. If the sales made by the plaintiff as trustee in 1946 had been made by a trustee of a trust created in the United Kingdom in terms of the trust involved in these proceedings they would have been in realization on and changes of investments within the provisions of the preceding paragraph herein and the gains and profits realized thereon would not have been subject to the United Kingdom income tax.

29. When the United Kingdom Tax Convention was entered into, under the United Kingdom Tax system there was an income tax (charged at a standard rate), a surtax, an excess profits tax and a so-called national defense contribution. During 1944 and 1945, under the United Kingdom system of taxation corporate profits arising to a United Kingdom corporation were subject to income tax at a standard rate of 50% and a national defense contribution of 5% (unless the excess profits tax on the corporate profits exceeded the national defense contribution) and such taxes were paid to the United Kingdom Treasury. When the corporation later

declared a dividend to its stockholders it was entitled to deduct therefrom an amount equal to tax at the standard rate on the amount of the dividend. A shareholder or a stockholder was not assessable to tax at the standard rate on the dividend, but was required to pay the surtax on the full amount of the dividend (including the amount of the standard tax attributable to the dividend) except that after the effective date of the Income Tax Convention between the United Kingdom and the United States a resident of the United States was exempted from the United Kingdom surtax in terms of Article VI (2) of the Convention.

30. During 1944 and 1945 the United Kingdom tax at the standard rate in respect of royalties from mines and other natural resources and rentals from real property derived from sources within the United Kingdom was imposed on the amount of such royalties and rentals after relevant deductions and allowances at 50%.

31. Prior to the United Kingdom Income Tax Convention, credits against the United Kingdom tax on account of foreign taxes paid were not allowed under United Kingdom law, except the following case which is not a case of tax credit, namely where income arises to a person resident in the United Kingdom from securities (other than Dominion or Colonial securities) out of the Kingdom, or from stocks or shares or certain other forms of possessions (other than Dominion or Colonial) out of the Kingdom and chargeable to income tax at the

standard rate though not remitted to this Kingdom, a deduction was allowed in computing the amount of the chargeable income of any sum which had been paid in respect of income tax in the place where the income had arisen. As a matter of judicial decision it has been held that to be so deductible the foreign tax must have been a tax on the income charged to the United Kingdom income tax. This however is not to be considered as a credit of tax against tax.

32. During 1944 and 1945 the United Kingdom did not impose a tax in respect of dividends and interest paid by a United States corporation to a non-resident of the United Kingdom (including residents of the United States), even though such United States corporation derived income from sources within the United Kingdom.

33. During 1944 and 1945 the United Kingdom did not impose taxes upon the accumulated or undistributed profits or surplus of a United States corporation except in the case of certain tax avoidance schemes.

Conclusions of Law

1. The capital gains involved in this case represent taxable income to the plaintiff herein and the plaintiff-trustee does not qualify for any exemption from taxation on that income.

2. The plaintiff is not entitled to recover in this action.

3. The complaint should be dismissed with costs taxed to the plaintiff.

Entered this 30th day of July, 1956.

/s/ OLIVER J. CARTER,
Judge.

Affidavit of Mail attached.

Lodged June 14, 1956.

[Endorsed]: Filed July 30, 1956.

In the United States District Court for the North-
ern District, of California, Southern Division

No. 33507

AMERICAN TRUST COMPANY, a Corporation,
as Trustee,

Plaintiff,

vs.

JAMES G. SMYTH, Collector of Internal Reve-
nue, and the UNITED STATES OF AMER-
ICA,

Defendants.

JUDGMENT

This cause came on for hearing before this Court without the intervention of a jury on March 22, 1955. Briefs were submitted by counsel on both sides and the case was argued orally before this Court on September 16, 1955.

The Court having heard the evidence and having considered the briefs and arguments of counsel, and having filed its findings of fact and conclusions of law herein in which it found the facts as stipulated by the parties and determined the law in favor of the defendants herein,

It Is Therefore Considered, Ordered and Adjudged, that judgment should be and hereby is entered in favor of the defendants James G. Smyth, Collector of Internal Revenue, and the United States of America, and that the plaintiffs complaint should be dismissed with costs taxed according to law.

Dated this 30th day of July, 1956, at San Francisco, California.

/s/ OLIVER J. CARTER,
Judge.

Lodged June 14, 1956.

[Endorsed]: Filed and entered July 30, 1956.

[Title of District Court and Cause.]

NOTICE OF APPEAL

Notice is hereby given that American Trust Company, appellant above named, hereby appeals to the United States Court of Appeals for the Ninth Circuit from the final judgment entered in this action on July 30, 1956.

/s/ HOWARD J. FINN,

/s/ THEODORE R. MEYER,
BROBECK, PHLEGER &
HARRISON,
Attorneys for Appellant.

/s/ MONTGOMERY B. ANGELL,
DAVIS, POLK, WARDWELL,
& KIENDL,
Of Counsel.

[Endorsed]: Filed September 14, 1956.

[Title of District Court and Cause.]

CERTIFICATE OF CLERK TO RECORD
ON APPEAL

I, C. W. Calbreath, Clerk of the United States District Court for the Northern District of California, hereby certify the foregoing and accompanying documents listed below, are the originals filed in this Court in the above-entitled case and constitute the record on appeal herein as designated by the attorneys for the appellant:

Excerpt from Docket Entries.

Complaint.

Answer.

Stipulation No. 2.

Memorandum for Judgment.

Findings of Fact and Conclusions of Law.

Judgment.

Notice of Appeal.

Appeal Bond.

Appellant's Designation of Record on Appeal.

In Witness Whereof, I have hereunto set my hand and affixed the seal of said District Court this 24th day of October, 1956.

[Seal] C. W. Calbreath,
Clerk.

By /s/ MARGARET P. BLAIR,
Deputy.

[Endorsed]: No. 15339. United States Court of Appeals for the Ninth Circuit. American Trust Company, a Corporation, Appellant, vs. James G. Smyth, Collector of Internal Revenue and United States of America, Appellees. Transcript of Record. Appeal from the United States District Court for the Northern District of California, Southern Division.

Filed October 24, 1956.

/s/ PAUL P. O'BRIEN,
Clerk of the United States Court of Appeals for the
Ninth Circuit.

In the United States Court of Appeals
for the Ninth Circuit

No. 15339

AMERICAN TRUST COMPANY, a Corporation,
as Trustee,

Appellant,

vs.

JAMES G. SMYTH, Collector of Internal Revenue
and UNITED STATES OF AMERICA,

Appellees.

STATEMENT OF POINTS

Pursuant to Rule 17(6) of this Court, appellant American Trust Company hereby files a concise statement of the points on which it intends to rely and a designation of all of the record which is material to the consideration of the appeal.

Statement of Points

1. The findings do not support the judgment, and therefore the Court erred in entering said judgment.
2. The findings compel a judgment for appellant as prayed in the Complaint, and therefore the Court erred in failing to enter such a judgment.

Dated: October 29, 1956.

/s/ THEODORE R. MEYER,

An Attorney for Appellant
American Trust Company.

[Endorsed]: Filed October 29, 1956.

